

# Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended.

Local Government Type <input checked="" type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input type="checkbox"/> Other		Local Government Name <b>City of Montrose</b>	County <b>Genesee</b>
Audit Date <b>6/30/05</b>	Opinion Date <b>9/29/05</b>	Date Accountant Report Submitted to State: <b>12/1/05</b>	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- |   |   |
|---|---|
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.   |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).  |
| <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No | 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).  |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.   |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).   |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.   |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).   |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).  |

**We have enclosed the following:**

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	✓		
Reports on individual federal financial assistance programs (program audits).			✓
Single Audit Reports (ASLGU).			✓

Certified Public Accountant (Firm Name) <b>Abraham &amp; Gaffney, P.C.</b>			
Street Address <b>3511 Coolidge Road Suite 100</b>	City <b>East Lansing</b>	State <b>MI</b>	ZIP <b>48823</b>
Accountant Signature <i>Abraham &amp; Gaffney, P.C.</i>		Date <i>11/30/05</i>	

**City of Montrose  
Genesee County, Michigan**

**FINANCIAL STATEMENTS**

**June 30, 2005**

City of Montrose  
Genesee County, Michigan  
CITY COUNCIL  
June 30, 2005

Eldon Dunklee	Mayor
Deborah Gross	Mayor Pro-Tem
Frank DeForke	Council Member
Norvill Landes	Council Member
Gene Powell	Council Member
Delana Vroman	Council Member
Scott Parks	Council Member

City of Montrose  
Genesee County, Michigan

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**ABRAHAM & GAFFNEY, P.C.**

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**INDEPENDENT AUDITOR'S REPORT**

To the Honorable Mayor and  
Members of the City Council  
City of Montrose  
Montrose, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Montrose, Michigan as of and for the year ended June 30, 2005, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of City of Montrose's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, based on our audit the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Montrose, Michigan as of June 30, 2005, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis and budgetary comparison information as identified in the table of contents are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming opinions on the financial statements that collectively comprise the City of Montrose's basic financial statements. The accompanying other supplementary information, as identified in the table of contents, is presented for the purpose of additional analysis and is not a required part of the basic financial statements. The other supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Abraham & Gaffney, P.C.*

ABRAHAM & GAFFNEY, P.C.  
Certified Public Accountants

September 29, 2005

## **City of Montrose**

### **Management's Discussion and Analysis**

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The following is a discussion and analysis of City of Montrose's (the City's) financial performance and position, providing an overview of the activities for the year ended June 30, 2005. This analysis should be read in conjunction with the *Independent Auditors Report* and with the City's financial statements, which follow this section.

#### **FINANCIAL HIGHLIGHTS**

##### **Government-wide:**

- Total net assets were \$4,021,277 (excluding component units).
- Governmental activities net assets were \$1,175,326.
- Business-type activity net assets were \$2,845,951.
- Component Unit net assets were \$193,214.

##### **Fund Level:**

- At the close of the fiscal year, the City's governmental funds reported a combined ending fund balance of \$1,181,700 with \$745,185 being reserved, designated, or otherwise earmarked for specific purposes (capital projects, debt service).
- The General Fund realized \$74,397 more in revenues and other financing sources than anticipated for the fiscal year. The General Fund operations expended \$31,680 more than appropriated.
- Overall, the General Fund balance increased by \$49,022 to \$198,985 - all undesignated and available for general purposes.

##### **Capital and Long-term Debt Activities:**

- The primary government had two (2) new debt issues for the fiscal year in the form of General Obligation Bonds and an installment purchase loan totaling \$824,055. The installment loan is for the purchase of a new backhoe for the City, while the bonds are for ongoing City improvements.
- The total long-term debt for the primary government was \$1,616,847, an increase of \$788,605 from the prior year.
- The City remains well below its authorized legal debt limit.
- The total additions to the capital asset schedule for the primary government were \$453,769 and included a new backhoe, improvements to the City's storm drain system, and the construction of the Orchard Street Storm Drains which is in progress.

#### **OVERVIEW OF THE FINANCIAL STATEMENTS**

This discussion and analysis is intended to serve as an introduction to the City's annual financial report. The annual financial report of the City consists of the following components: 1) *Independent Auditor's Report*; 2) *Management's Discussion and Analysis* and 3) the *Basic Financial Statements* (government-wide financial statements, fund financial statements, notes to the financial statements), 4) *Required Supplementary Information* such as budget to actual comparisons for the General Fund and major Special Revenue Funds, and 5) *Other Supplementary Information* including combining financial statements for all nonmajor governmental funds and other funds and other financial data.

##### **Government-wide Financial Statements (Reporting the City as a Whole)**

The set of government-wide financial statements are made up of the Statement of Net Assets and the Statement of Activities, which report information about the City as a whole, and about its activities. Their purpose is to assist in answering the question, is the City, in its entirety, better or worse off as a result of this fiscal year's activities? These statements, which include all nonfiduciary assets and liabilities, are reported on the *accrual basis of accounting*, similar to a private business. This means revenues are accounted for when they are *earned* and expenses are accounted for when *incurred*, regardless of when the actual cash is received or disbursed.

## City of Montrose

### Management's Discussion and Analysis

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The Statement of Net Assets (page 1) presents all of the City's assets and liabilities, recording the difference between the two as "net assets". Over time, increases or decreases in net assets measure whether the City's financial position is improving or deteriorating.

The Statement of Activities (page 2) presents information showing how the City's net assets changed during 2004/2005. All changes in net assets are reported based on the period for which the underlying events giving rise to the change occurs, regardless of the timing of related cash flows. Therefore, revenue and expenses are reported in these statements for some items that will only result in cash flows in future financial periods, such as uncollected taxes and earned but unused employee vacation leave.

Both statements report the following activities:

- **Governmental Activities** - Most of the City's basic services are reported under this category. Taxes, charges for services and intergovernmental revenue primarily fund these services. Most of the City's general government departments, public safety, public works, economic development, city improvements, recreation activities, and other City wide elected official operations are reported under these activities.
- **Business-type Activities** - These activities operate like private businesses. The City charges fees to recover the cost of the services provided. The Sewer System and Water System are examples of these activities.
- **Discretely Presented Component Unit** - The discretely presented component unit (Downtown Development Authority) is a legally separate organization for which the City Council and Administration appoints a majority of the organization's policy board and there is a degree of financial accountability to the City.

As stated previously, the government-wide statements report on an *accrual* basis of accounting. However, the governmental funds report on a *modified accrual* basis. Under modified accrual accounting, revenues are recognized when they are measurable and available to pay obligations of the fiscal period; expenditures are recognized when they are due to be paid from available resources.

Because of the different basis of accounting between the fund statements (described below) and the government-wide statements, pages 5 and 8 present reconciliations between the two statement types. The following summarizes the impact of transitioning from modified accrual to full accrual accounting:

- Capital assets used in governmental activities (depreciation) are not reported on the fund financial statements of the governmental fund. Capital assets and depreciation expense are reported on the government-wide statements.
- Capital outlay spending results in capital assets on the government-wide statements, but is reported as expenditures on the fund financial statements of the governmental funds.
- Long-term liabilities, such as amounts accrued for sick and annual leave (compensated absences), etc. appear as liabilities on the government-wide statements; however they will not appear on the fund financial statements unless current resources are used to pay a specific obligation.
- Long-term debt proceeds are reported as liabilities on the government-wide statements, but are recorded as other financing sources on the fund financial statements.

#### **Fund Financial Statements (Reporting the City's Major Funds)**

The fund financial statements, which begin on page 3, provide information on the City's significant (major) funds, and aggregated nonmajor funds. A fund is a fiscal and accounting entity with a self-balancing set of accounts that the City uses to keep track of specific sources of funding and spending for a particular purpose. Traditional users of governmental financial statements will find the Fund Financial Statements presentation more familiar.

## City of Montrose

### Management's Discussion and Analysis

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The *basic financial statements* report major funds as defined by the Government Accounting Standards Board (GASB) in separate columns. Statement 34 defines a "major fund" as the General Fund, and any governmental or enterprise fund which has either total assets, total liabilities, total revenues or total expenditures/expenses that equal at least ten (10) percent of those categories for either the governmental funds or the enterprise funds and where the individual fund total also exceeds five (5) percent of those categories for governmental and enterprise funds combined. The major funds for City of Montrose include the General Fund, the Major Street Fund, the Local Street Fund, the Capital Projects Fund, the Sewer System Fund and the Water System Fund. All other funds are classified as nonmajor funds and are reported in aggregate by the applicable fund type.

The City's funds are divided into three categories - governmental, proprietary, and fiduciary - and use different accounting approaches:

- **Governmental Funds** - Most of the City's basic services are reported in the governmental funds. The focus of these funds is how cash and other financial assets that can be readily converted to cash, flow in and out during the course of the fiscal year and how the balances left at year-end are available for spending on future services. Consequently, the governmental fund financial statements provide a detailed short-term view that helps determine whether there are more or fewer financial resources that may be expended in the near future to finance the City's programs. Governmental funds include the *General Fund*, as well as *Special Revenue Funds* (use of fund balance is restricted, e.g. major street, local street, and depot funds), *Capital Projects Funds* (used to report major capital acquisitions and construction, e.g. the Capital Projects Fund), and *Debt Service Funds* (accounts for resources used to pay long-term debt principal and interest e.g. voted bonds and non-voted bonds funds).
- **Proprietary Funds** - Services for which the City charges customers (whether outside the City structure or a City department) a fee are generally reported in proprietary funds. Proprietary funds use the same *accrual* basis of accounting used in the government-wide statements and by private business. There are two types of proprietary funds. *Enterprise funds* report activities that provide supplies and/or services to the general public. An example is the Sewer System Fund.
- **Fiduciary Funds** - The City may act as a trustee or fiduciary in certain instances. It is also responsible for other assets that, because of trust arrangements, can only be used for the trust beneficiaries. The City's fiduciary activities are reported in the separate Statement of Net Assets on page 13. These funds, which include trust and agency funds, are reported using the accrual basis of accounting. The government-wide statements *exclude* the fiduciary fund activities and balances because these assets are not available to the City to fund its operations.

#### Notes to the Financial Statements

The Notes to the Financial Statements provide additional information that is essential to a full understanding of the detail provided in the government-wide and fund financial statements. The Notes can be found beginning on page 14 of this report.

#### Required Supplementary Information

Following the Basic Financial Statements is additional Required Supplementary Information (RSI), which further explains and supports the information in the financial statements. RSI includes budgetary comparison schedules for the General Fund and the major special revenue funds.

#### Other Supplementary Information

Other Supplementary Information includes combining financial statements for nonmajor governmental funds. These funds are added together and are presented in aggregate single columns in the appropriate basic financial statements.



**City of Montrose**  
**Management's Discussion and Analysis**

**FINANCIAL ANALYSIS OF THE CITY AS A WHOLE**

As previously stated, City of Montrose combined net assets were \$4,021,277 at the end of this fiscal year's operations. The net assets of the governmental activities were \$1,175,326; the business-type activities were \$2,845,951.

**Net Assets as of June 30, 2005 and 2004**

	Governmental Activities		Business-type Activities		Total Primary Government	
	2005	2004	2005	2004	2005	2004
Current and Other Assets	\$ 1,341,875	\$ 485,297	\$ 1,786,301	\$ 2,104,629	\$ 3,128,176	\$ 2,589,926
Capital Assets	<u>724,332</u>	<u>293,431</u>	<u>1,909,294</u>	<u>1,994,295</u>	<u>2,633,626</u>	<u>2,287,726</u>
<b>Total Assets</b>	<b><u>\$ 2,066,207</u></b>	<b><u>\$ 778,728</u></b>	<b><u>\$ 3,695,595</u></b>	<b><u>\$ 4,098,924</u></b>	<b><u>\$ 5,761,802</u></b>	<b><u>\$ 4,877,652</u></b>
Current Liabilities	\$ 111,647	\$ 70,300	\$ 95,450	\$ 93,332	\$ 207,097	\$ 163,632
Noncurrent Liabilities	<u>779,234</u>	<u>1,535</u>	<u>754,194</u>	<u>790,420</u>	<u>1,533,428</u>	<u>791,955</u>
<b>Total Liabilities</b>	<b><u>\$ 890,881</u></b>	<b><u>\$ 71,835</u></b>	<b><u>\$ 849,644</u></b>	<b><u>\$ 883,752</u></b>	<b><u>\$ 1,740,525</u></b>	<b><u>\$ 955,587</u></b>
<b>Net Assets</b>						
Invested in Capital Assets (Net of related debt)	\$ 643,384	\$ 293,431	\$ 1,129,294	\$ 1,179,295	\$ 1,772,678	\$ 1,472,726
Restricted	972,169	150,501	67,059	45,028	1,039,228	195,529
Unrestricted	<u>( 440,227 )</u>	<u>262,961</u>	<u>1,649,598</u>	<u>1,990,849</u>	<u>1,209,371</u>	<u>2,253,810</u>
<b>Total Net Assets</b>	<b><u>\$ 1,175,326</u></b>	<b><u>\$ 706,893</u></b>	<b><u>\$ 2,845,951</u></b>	<b><u>\$ 3,215,172</u></b>	<b><u>\$ 4,021,277</u></b>	<b><u>\$ 3,922,065</u></b>

The following condensed financial information was derived from the government-wide Statement of Activities and reflects how the City's primary government net assets changed during the fiscal year:

**Changes in Net Assets for the Fiscal Year Ending June 30, 2005 and 2004**

	Governmental Activities		Business-type Activities		Total	
	2005	2004	2005	2004	2005	2004
<b>Revenues</b>						
Program Revenues						
Charges for Services	\$ 142,438	\$ 240,180	\$ 554,764	\$ 641,298	\$ 697,202	\$ 881,478
Grants and Contributions	112,625	143,247	81,417	813	194,042	144,060
General Revenues						
Property Taxes	402,583	369,871	-	-	402,583	369,871
State Shared Revenue	194,393	203,769	-	-	194,393	203,769
Investment Earnings	7,279	4,378	24,180	12,681	31,459	17,059
Miscellaneous	38,817	3,937	194	10,059	39,011	13,996
Transfers	<u>485,600</u>	<u>-</u>	<u>( 485,600 )</u>	<u>-</u>	<u>-0-</u>	<u>-0-</u>
<b>Total Revenues</b>	<b>1,383,735</b>	<b>965,382</b>	<b>174,955</b>	<b>664,851</b>	<b>1,558,690</b>	<b>1,630,233</b>

**City of Montrose**  
**Management's Discussion and Analysis**

**Changes in Net Assets for the Fiscal Year Ending June 30, 2005 and 2004 - continued**

	Governmental Activities		Business-type Activities		Total	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
<b>Expenses</b>						
General Govt.	\$ 324,654	\$ 330,511	\$ -	\$ -	\$ 324,654	\$ 330,511
Public Safety	269,477	272,418	-	-	269,477	272,418
Public Works	265,332	203,259	-	-	265,332	203,259
Community and Economic Develop.	42,366	4,113	-	-	42,366	4,113
Recreation and Cultural	15,390	17,840	-	-	15,390	17,840
Other	<u>5,940</u>	<u>-</u>	<u>544,176</u>	<u>563,401</u>	<u>550,116</u>	<u>563,401</u>
<b>Total Expenses</b>	<b><u>923,159</u></b>	<b><u>828,141</u></b>	<b><u>544,176</u></b>	<b><u>563,401</u></b>	<b><u>1,467,335</u></b>	<b><u>1,391,542</u></b>
<b>Increase in Net Assets</b>	<b>460,576</b>	<b>137,241</b>	<b>( 369,221 )</b>	<b>101,450</b>	<b>91,355</b>	<b>238,691</b>
Net Assets - Beginning	706,893	569,652	3,215,172	3,113,722	3,922,065	3,683,374
Prior Period Adjustment	<u>7,857</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>7,857</u>	<u>-0-</u>
<b>Net Assets - Ending</b>	<b><u>\$ 1,175,326</u></b>	<b><u>\$ 706,893</u></b>	<b><u>\$ 2,845,951</u></b>	<b><u>\$ 3,215,172</u></b>	<b><u>\$ 4,021,277</u></b>	<b><u>\$ 3,922,065</u></b>

**Governmental Activities:**

The result of 2004/2005 governmental activity was an increase of \$460,576 in net assets to \$1,175,326. Of the total governmental activities' net assets, \$643,384 is invested in capital assets less related debt, \$972,169 is reported as restricted, meaning these assets are legally committed for a specific purpose through statute, or by another authority outside the City government. The balance of \$(440,227) is listed as unrestricted.

**Revenues:**

The three largest revenue categories were transfers in from business-type funds at 35%, property taxes at 29%, and state shared revenue at 14%. The City levied a property tax millage for the year ended June 30, 2005, for general government operations at 17.7501 mills, which is not assigned to any particular activity. State shared revenue, the third largest source of governmental activity revenue, is also not assigned to any particular activity.

**Expenses:**

General government is the largest governmental activity, expending approximately 35% of the governmental activities total and includes general government departments (e.g. council, community promotions, city manager, elections, general administration, assessor, city hall maintenance, and cemetery operations). Public Safety is the second largest area, expending approximately 29% of the governmental activities total on law enforcement, fire protection and code enforcement. Public Works expended approximately 28% of the governmental activities total and would be higher if capital outlay charged to this function in the funds were not shown as capital assets in the government-wide financial statements.

## City of Montrose

### Management's Discussion and Analysis

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#### **Business-type Activities:**

Net assets in business-type activities decreased by \$369,221 during fiscal year 2004/2005. Of the business-type activities' net assets, \$1,129,294 is invested in capital assets net of related debt; \$67,059 is reported as restricted, meaning these assets are legally committed for a specific purpose through statute or by another authority outside the City government, and the balance of \$1,649,598 is listed as unrestricted, having no legal commitment.

#### **FINANCIAL ANALYSIS OF THE CITY'S MAJOR AND NON MAJOR FUNDS**

As the City completed 2004/2005, its governmental funds reported *combined* fund balances of \$1,181,700. This is a net increase of \$926,903. The net changes are summarized in the following chart:

	General Fund	Major Street	Local Street	Capital Projects	Nonmajor Governmental Funds	Total Governmental Funds
<b>Fund Balance (deficit) 06/30/04</b>	\$ 149,963	\$ 150,164	\$( 66,934 )	\$ -	\$ 21,604	\$ 254,797
<b>Fund Balance 06/30/05</b>	\$ 198,985	\$ 178,888	\$ 50,174	\$ 743,107	\$ 10,546	\$ 1,181,700
<b>Net Change</b>	\$ 49,022	\$ 28,724	\$ 117,108	\$ 743,107	\$( 11,058 )	\$ 926,903

#### **General Fund:**

The General Fund is the chief operating fund of the City. Unless otherwise required by statute, contractual agreement or Council policy, all City revenues and expenditures are recorded in the General Fund. As of June 30, 2005, the General Fund reported a fund balance of \$198,985. This amount is an increase of \$49,022 from the fund balance of \$149,963 reported as of June 30, 2004. The 2004/2005 original budget had called for a \$16,500 increase of fund balance.

The General Fund 2004/2005 expenditures exceeded 2004/2005 revenues by \$81,018 due in large part to the City taking out an installment loan for a new backhoe.

#### **General Fund Budgetary Highlights:**

The City of Montrose's budget is a dynamic document. Although adopted in May (prior to the start of the year), the budget is routinely amended during the course of the year to reflect changing operational demands.

Actual General Fund revenue and other financing sources totaled \$858,488, \$74,397 above the final amended budget. There were some wide variations in individual revenue accounts reflecting the tightening national and local economy.

The \$74,397 excess in budgeted General Fund Revenue was due to loan proceeds received to pay for the new backhoe.

The City's expenditure budget was increased by \$19,801 (3% above the original budget) during 2004/2005.

Actual City expenditures for 2004/2005 were \$31,680 above the amended budget and \$51,484 above the original budget.

## **City of Montrose**

### **Management's Discussion and Analysis**

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The General Fund department that expended more than planned expenditures was the Department of Public Works (\$57,570). This budget variance was due to the requirement to report the financed purchase of the backhoe as an expenditure of the current period. This reporting requirement was not considered when the original budget was adopted or amended.

#### **Major Street Fund**

As of June 30, 2005, the Major Street Fund reported a fund balance of \$178,888, which is an increase of \$28,724 from the prior year. The total fund balance is undesignated/unreserved.

#### **Local Street Fund**

As of June 30, 2005, the Local Street Fund reported a fund balance \$50,174, which is an increase of \$117,108 from the prior year. The total fund balance is undesignated/unreserved. The reason for the significant increase in fund balance was a transfer in from the Sewer System Fund of \$430,000.

#### **Capital Projects Fund**

As of June 30, 2005, the Capital Projects Fund reported a fund balance \$743,107. This fund was established in the current year with the purpose of making capital improvements to the City. The total fund balance is designated for capital expenditures.

#### **Business-type Activities Funds**

As the City completed 2004/2005, its business-type activities funds reported *combined* net assets of \$2,845,951. This is a net decrease of \$369,221. The net changes are summarized in the following chart.

	<b>Sewer System Fund</b>	<b>Water System Fund</b>	<b>Total</b>
<b>Net Assets 06/30/04</b>	\$ 1,940,531	\$ 1,274,641	\$ 3,215,172
<b>Net Assets 06/30/05</b>	\$ 1,501,731	\$ 1,344,220	\$ 2,845,951
<b>Net Change</b>	\$ ( 438,800 )	\$ 69,579	\$ ( 369,221 )

#### **Sewer System Fund:**

As of June 30, 2005, the Sewer Fund reported net assets of \$1,501,731, a decrease of \$438,800 from the prior year. The total net assets balance is undesignated/unreserved. The reason for the significant decrease of net assets was a transfer out to the Local Street Fund of \$430,000.

#### **Water System Fund:**

As of June 30, 2005, the Water System Fund reported a fund balance of \$1,344,220, an increase of \$69,579 from the prior year. \$67,059 is restricted for debt service, while the remaining balance is undesignated/unreserved.

**City of Montrose**  
**Management's Discussion and Analysis**

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**CAPITAL ASSETS AND DEBT ADMINISTRATION**

Capital Assets - At the end of Fiscal Year 2004/2005, the City had invested \$2,633,626, and \$126,401 for the component unit, net of accumulated depreciation, in a broad range of capital assets (see table below). Additional information related to capital assets is detailed in Note D of the Financial Statements. Net Book value of capital assets at June 30, 2005 was as follows:

	<b>Governmental Activities</b>	<b>Business-type Activities</b>	<b>Component Unit DDA</b>	<b>Total</b>
<b>Land</b>	\$ 99,000	\$ 50,620	\$ 38,000	\$ 187,620
<b>Construction in progress</b>	88,994	11,764	-	100,758
<b>Vehicles and equipment, net</b>	112,213	-	-	112,213
<b>Sewer system, net</b>	-	707,444	-	707,444
<b>Water system, net</b>	-	1,139,466	-	1,139,466
<b>Infrastructure Streets &amp; Bridges, net</b>	424,125	-	88,401	512,526
<b>Capital assets, net</b>	<b>\$ 724,332</b>	<b>\$ 1,909,294</b>	<b>\$ 126,401</b>	<b>\$ 2,760,027</b>

Long-term Debt - As of June 30, 2005, the City had \$1,616,847 in loans outstanding for the primary government. This level of net obligation is \$788,605 more than the obligation recorded as of June 30, 2004, principally due to the 2005 General Obligation Bonds.

**Outstanding Debt as of June 30, 2005:**

<b>Primary Government</b>	<b><u>July 1, 2004</u></b>	<b><u>Additions</u></b>	<b><u>Reductions</u></b>	<b><u>June 30, 2005</u></b>
Governmental Activities				
General Obligation Bonds	\$ -	\$ 750,000	\$ -	\$ 750,000
Installment Loan	-	74,055	-	74,055
Compensated Absences	2,046	2,434	-	4,480
Business-type Activities				
Water Revenue Bonds	815,000	-	35,000	780,000
Compensated Absences	11,196	-	2,884	8,312
<b>Total Reporting Entity</b>	<b>\$ 828,242</b>	<b>\$ 826,489</b>	<b>\$ 37,884</b>	<b>\$ 1,616,847</b>

A more detailed discussion of the City's long-term debt obligations is presented in Note E to the financial statements.

**ECONOMIC OUTLOOK:**

- Property tax revenue has not kept pace with inflation.
- Health and dental insurance premiums are rising much faster than the rate of inflation.
- Retirement costs are increasing due to poor stock market performance over the last several years.
- Utility costs are rising faster than the rate of inflation.
- Hazard/Liability Insurance costs are rising faster than the rate of inflation.

These factors were considered in adopting the Budget for 2005/2006. A usage of \$2,878 of the City's fund balance was included to balance the General Fund Budget, although it is estimated that the deficit will be less as the City continues to look for ways to increase efficiencies and reduce the cost of doing business.

**City of Montrose**  
**Management's Discussion and Analysis**

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**CONTACTING THE CITY**

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If there are questions about this report, or a need for additional information, contact the City of Montrose's Office at (810) 639-6168.

## **BASIC FINANCIAL STATEMENTS**

City of Montrose

STATEMENT OF NET ASSETS

June 30, 2005

	Primary Government			
	Governmental Activities	Business-type Activities	Total	Component Unit
ASSETS				
Current assets				
Cash and cash equivalents	\$ 1,190,465	\$ 1,609,757	\$ 2,800,222	\$ 67,088
Receivables	127,243	98,301	225,544	-
Due from other governmental units	24,167	-	24,167	-
Total current assets	1,341,875	1,708,058	3,049,933	67,088
Noncurrent assets				
Cash - restricted	-	78,243	78,243	-
Capital assets not being depreciated	187,994	62,384	250,378	-
Capital assets, net of accumulated depreciation	536,338	1,846,910	2,383,248	126,401
Total noncurrent assets	724,332	1,987,537	2,711,869	126,401
TOTAL ASSETS	2,066,207	3,695,595	5,761,802	193,489
LIABILITIES				
Current liabilities				
Accounts payable	49,655	49,219	98,874	275
Accrued liabilities	6,751	929	7,680	-
Accrued interest payable	5,940	9,500	15,440	-
Current portion of compensated absences	2,863	802	3,665	-
Current portion of long-term debt	46,438	35,000	81,438	-
Total current liabilities	111,647	95,450	207,097	275
Noncurrent liabilities				
Compensated absences	1,617	7,510	9,127	-
Customer deposits	-	1,684	1,684	-
Noncurrent portion of long-term debt	777,617	745,000	1,522,617	-
Total noncurrent liabilities	779,234	754,194	1,533,428	-0-
TOTAL LIABILITIES	890,881	849,644	1,740,525	275
NET ASSETS				
Invested in capital assets, net of related debt	643,384	1,129,294	1,772,678	126,401
Restricted for:				
Streets	229,062	-	229,062	-
Debt service	-	67,059	67,059	-
Capital projects	743,107	-	743,107	-
Unrestricted	(440,227)	1,649,598	1,209,371	66,813
TOTAL NET ASSETS	\$ 1,175,326	\$ 2,845,951	\$ 4,021,277	\$ 193,214

See accompanying notes to financial statements.



City of Montrose

STATEMENT OF ACTIVITIES

Year Ended June 30, 2005

Functions/Programs	Program Revenues			Net (Expense) Revenue and Changes in Net Assets		
	Expenses	Charges for Services		Primary Government		Component Unit
			Operating Grants and Contributions	Governmental Activities	Business-type Activities	Total
Primary government:						
Governmental activities:						
General government	\$ 324,654	\$ 18,714	\$ 23,115	\$ (282,825)	\$ -	\$ (282,825)
Public safety	269,477	16,710	-	(252,767)	-	(252,767)
Public works	265,332	107,014	89,510	(68,808)	-	(68,808)
Community and economic development	42,366	-	-	(42,366)	-	(42,366)
Recreation and cultural	15,390	-	-	(15,390)	-	(15,390)
Interest on long-term debt	5,940	-	-	(5,940)	-	(5,940)
Total governmental activities	923,159	142,438	112,625	(668,096)	-0-	(668,096)
Business-type activities:						
Sewer system	257,101	292,706	610	-	36,215	36,215
Water system	287,075	262,058	80,807	-	55,790	55,790
Total business-type activities	544,176	554,764	81,417	-0-	92,005	92,005
Total primary government	\$ 1,467,335	\$ 697,202	\$ 194,042	(668,096)	92,005	(576,091)
Component unit:						
Downtown Development Authority	\$ 7,027	\$ -0-	\$ 334	-	-	-0-
						(6,693)
General revenues and transfers:						
Property taxes				402,583	-	402,583
State shared revenues				194,393	-	194,393
Investment earnings				7,279	24,180	31,459
Miscellaneous				38,817	194	39,011
Transfers				485,600	(485,600)	-0-
Total general revenues and transfers				1,128,672	(461,226)	667,446
						52,975
Change in net assets				460,576	(369,221)	91,355
						46,282
Net assets, beginning of the year				706,893	3,215,172	3,922,065
						124,537
Prior period adjustment				7,857	-	7,857
						22,395
Net assets, end of the year				\$ 1,175,326	\$ 2,845,951	\$ 4,021,277
						\$ 193,214

See accompanying notes to financial statements.

City of Montrose

GOVERNMENTAL FUNDS BALANCE SHEET

June 30, 2005

	General	Major Street	Local Street
<b>ASSETS</b>			
Cash and cash equivalents	\$ 216,844	\$ 161,744	\$ 56,724
Receivables			
Accounts	678	18,018	4,778
Special assessments	-	23,578	80,191
Due from other governmental units	24,167	-	-
<b>TOTAL ASSETS</b>	<u>\$ 241,689</u>	<u>\$ 203,340</u>	<u>\$ 141,693</u>
<b>LIABILITIES AND FUND BALANCES</b>			
<b>LIABILITIES</b>			
Payables			
Accounts	\$ 37,232	\$ 181	\$ 10,742
Accrued wages	5,472	693	586
Deferred revenue	-	23,578	80,191
<b>TOTAL LIABILITIES</b>	42,704	24,452	91,519
<b>FUND BALANCES</b>			
Reserved for debt service	-	-	-
Designated for capital expenditures	-	-	-
Unreserved			
Undesignated, reported in:			
General fund	198,985	-	-
Special revenue funds	-	178,888	50,174
<b>TOTAL FUND BALANCES</b>	<u>198,985</u>	<u>178,888</u>	<u>50,174</u>
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<u>\$ 241,689</u>	<u>\$ 203,340</u>	<u>\$ 141,693</u>

See accompanying notes to financial statements.

Capital Projects	Nonmajor Governmental Funds	Total Governmental Funds
\$ 743,107	\$ 12,046	\$ 1,190,465
-	-	23,474
-	-	103,769
-	-	24,167
<u>\$ 743,107</u>	<u>\$ 12,046</u>	<u>\$ 1,341,875</u>

\$ -	\$ 1,500	\$ 49,655
-	-	6,751
-	-	103,769

-0-	1,500	160,175
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-	2,078	2,078
743,107	-	743,107

-	-	198,985
-	8,468	237,530

743,107	10,546	1,181,700
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<u>\$ 743,107</u>	<u>\$ 12,046</u>	<u>\$ 1,341,875</u>
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City of Montrose

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET  
TO THE STATEMENT OF NET ASSETS

June 30, 2005

**Total fund balance - governmental funds** **\$ 1,181,700**

Amounts reported for the governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources  
and therefore are not reported as assets in the governmental funds.

The cost of capital assets is	\$ 1,062,749	
Accumulated depreciation is	<u>(338,417)</u>	
Capital assets, net		724,332

Long-term receivables are not available to pay for current period expenditures  
and are therefore deferred in the funds. These consist of:

Deferred revenue	103,769
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Long-term liabilities are not due and payable in the current period and  
therefore are not reported in the Governmental Funds Balance Sheet.  
Long-term liabilities at year-end consist of:

Direct City obligations	824,055	
Accrued interest payable	5,940	
Compensated absences	<u>4,480</u>	
		<u>(834,475)</u>

**Net assets of governmental activities** **\$ 1,175,326**

See accompanying notes to financial statements.

City of Montrose

Governmental Funds

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

Year Ended June 30, 2005

	General	Major Street	Local Street
REVENUES			
Taxes	\$ 409,108	\$ -	\$ -
Licenses and permits	21,776	-	-
Intergovernmental	194,393	89,576	56,876
Charges for services	53,952	-	-
Fines and forfeits	6,773	-	-
Interest and rents	39,757	1,762	1,126
Other	2,689	7,859	45,553
TOTAL REVENUES	728,448	99,197	103,555
EXPENDITURES			
General government	318,581	-	-
Public safety	269,477	-	-
Public works	199,672	50,797	436,123
Community and economic development	6,346	-	-
Recreation and cultural	15,390	-	-
TOTAL EXPENDITURES	809,466	50,797	436,123
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	(81,018)	48,400	(332,568)
OTHER FINANCING SOURCES (USES)			
Bond and loan proceeds	74,055	-	-
Bond issuance costs	-	-	-
Transfers in	55,985	-	449,676
Transfers out	-	(19,676)	-
TOTAL OTHER FINANCING SOURCES (USES)	130,040	(19,676)	449,676
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES AND OTHER FINANCING USES	49,022	28,724	117,108
Fund balances (deficit), beginning of year	149,963	150,164	(66,934)
Fund balances, end of year	\$ 198,985	\$ 178,888	\$ 50,174

See accompanying notes to financial statements.

Capital Projects	Nonmajor Governmental Funds	Total Governmental Funds
\$ -	\$ -	\$ 409,108
-	-	21,776
-	-	340,845
-	-	53,952
-	-	6,773
607	155	43,407
-	23,115	79,216
607	23,270	955,077
-	-	318,581
-	-	269,477
-	-	686,592
-	36,020	42,366
-	-	15,390
-0-	36,020	1,332,406
607	(12,750)	(377,329)
750,000	-	824,055
(5,423)	-	(5,423)
-	2,077	507,738
(2,077)	(385)	(22,138)
742,500	1,692	1,304,232
743,107	(11,058)	926,903
-	21,604	254,797
\$ 743,107	\$ 10,546	\$ 1,181,700

City of Montrose

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND  
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES

Year Ended June 30, 2005

**Net change in fund balances - total governmental funds** \$ 926,903

Amounts reported for governmental activities in the statement of activities are different because:

Capital outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts are:

Capital outlay	\$ 442,005
Depreciation expense	<u>(18,961)</u>

Excess of capital outlay over depreciation expense	423,044
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Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	(56,942)
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Repayment of long-term debt and borrowing of long-term debt is reported as expenditures and other financing sources in governmental funds, but the repayment reduces long-term liabilities and the borrowings increases long-term liabilities in the statement of net assets. In the current year, these amounts consist of:

Bond and loan proceeds	(824,055)
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Some items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These activities consist of:

(Increase) in accrued interest payable	(5,940)
(Increase) in accrued compensated absences	<u>(2,434)</u>
	<u>(8,374)</u>

<b>Change in net assets of governmental activities</b>	<u><u>\$ 460,576</u></u>
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See accompanying notes to financial statements.

## City of Montrose

## Proprietary Funds

## STATEMENT OF NET ASSETS

June 30, 2005

	Sewer System	Water System	Total
<b>ASSETS</b>			
Current assets			
Cash and cash equivalents	\$ 727,249	\$ 882,508	\$ 1,609,757
Accounts receivable	43,658	54,643	98,301
Total current assets	770,907	937,151	1,708,058
Noncurrent assets			
Cash - restricted	-	78,243	78,243
Capital assets not being depreciated	56,088	6,296	62,384
Capital assets, net of accumulated depreciation	707,444	1,139,466	1,846,910
Total noncurrent assets	763,532	1,224,005	1,987,537
<b>TOTAL ASSETS</b>	1,534,439	2,161,156	3,695,595
<b>LIABILITIES</b>			
Current liabilities			
Accounts payable	28,193	21,026	49,219
Wages payable	359	570	929
Accrued liabilities	-	9,500	9,500
Current portion of compensated absences	401	401	802
Current portion of long-term debt	-	35,000	35,000
Total current liabilities	28,953	66,497	95,450
Noncurrent liabilities			
Payable from restricted cash -			
Customer deposits payable	-	1,684	1,684
Compensated absences	3,755	3,755	7,510
Bonds payable	-	745,000	745,000
Total noncurrent liabilities	3,755	750,439	754,194
<b>TOTAL LIABILITIES</b>	32,708	816,936	849,644
<b>NET ASSETS</b>			
Invested in capital assets, net of related debt	763,532	365,762	1,129,294
Restricted for debt service	-	67,059	67,059
Unrestricted	738,199	911,399	1,649,598
<b>TOTAL NET ASSETS</b>	<u>\$ 1,501,731</u>	<u>\$ 1,344,220</u>	<u>\$ 2,845,951</u>

See accompanying notes to financial statements.



## City of Montrose

## Proprietary Funds

## STATEMENT OF REVENUE, EXPENSES, AND CHANGES IN FUND NET ASSETS

Year Ended June 30, 2005

	Sewer System	Water System	Total
OPERATING REVENUES			
Charges for services			
User charges	\$ 282,264	\$ 246,328	\$ 528,592
Tap in fees	10,442	3,150	13,592
Other	80	114	194
TOTAL OPERATING REVENUES	292,786	249,592	542,378
OPERATING EXPENSES			
Salaries and wages	17,932	26,380	44,312
Fringe benefits	17,431	18,740	36,171
Contractual service	141,299	140,111	281,410
Supplies	3,089	3,973	7,062
Utilities	2,830	4,458	7,288
Insurance	3,655	4,151	7,806
Repairs and maintenance	7,942	4,987	12,929
Other	5,021	5,101	10,122
Depreciation	57,902	38,863	96,765
TOTAL OPERATING EXPENSES	257,101	246,764	503,865
OPERATING INCOME	35,685	2,828	38,513
NONOPERATING REVENUES (EXPENSES)			
Hydrant assessments	-	12,580	12,580
Special assessments	610	80,807	81,417
Interest revenue	10,505	13,675	24,180
Paying agent fees	-	(1,000)	(1,000)
Interest expense	-	(39,311)	(39,311)
TOTAL NONOPERATING REVENUES (EXPENSES)	11,115	66,751	77,866
INCOME BEFORE TRANSFERS	46,800	69,579	116,379
TRANSFER OUT	(485,600)	-	(485,600)
CHANGE IN NET ASSETS	(438,800)	69,579	(369,221)
Net assets, beginning of year	1,940,531	1,274,641	3,215,172
Net assets, end of year	\$ 1,501,731	\$ 1,344,220	\$ 2,845,951

See accompanying notes to financial statements.

City of Montrose

Proprietary Funds

STATEMENT OF CASH FLOWS

Year Ended June 30, 2005

	Sewer System	Water System	Total
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Cash receipts from customers	\$ 293,525	\$ 244,956	\$ 538,481
Cash receipts from interfund activity	117,919	75,505	193,424
Cash paid to suppliers	(214,129)	(155,000)	(369,129)
Cash paid for employee benefits	(18,873)	(20,620)	(39,493)
Cash paid to employees	(18,078)	(26,707)	(44,785)
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>160,364</b>	<b>118,134</b>	<b>278,498</b>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>			
Transfer out	(485,600)	-	(485,600)
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>			
Hydrant assessments	-	12,580	12,580
Special assessments	610	80,807	81,417
Paying agent fees	-	(1,000)	(1,000)
Interest expense	-	(39,311)	(39,311)
Capital purchases	(5,468)	(6,296)	(11,764)
Payments on borrowings	-	(35,000)	(35,000)
<b>NET CASH PROVIDED (USED) BY CAPITAL AND RELATED FINANCING ACTIVITIES</b>	<b>(4,858)</b>	<b>11,780</b>	<b>6,922</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Interest revenue	10,505	13,675	24,180
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>(319,589)</b>	<b>143,589</b>	<b>(176,000)</b>
Cash and cash equivalents, beginning of year	1,046,838	817,162	1,864,000
Cash and cash equivalents, end of year	<u>\$ 727,249</u>	<u>\$ 960,751</u>	<u>\$ 1,688,000</u>

See accompanying notes to financial statements.

City of Montrose

Proprietary Funds

STATEMENT OF CASH FLOWS - CONTINUED

Year Ended June 30, 2005

	Sewer System	Water System	Total
Reconciliation of operating income to net cash provided by operating activities			
Operating income	\$ 35,685	\$ 2,828	\$ 38,513
Adjustments to reconcile operating income to net cash provided by operating activities			
Depreciation	57,902	38,863	96,765
(Increase) decrease in accounts receivable	739	(4,296)	(3,557)
Decrease in due from other funds	117,919	75,505	193,424
Increase (decrease) in accounts payable	(2,939)	7,966	5,027
(Decrease) in wages payable	(146)	(327)	(473)
(Decrease) in other accrued liabilities	-	(438)	(438)
(Decrease) in compensated absences	(1,442)	(1,442)	(2,884)
(Decrease) in customer deposits	-	(340)	(340)
(Decrease) in due to other funds	(47,354)	(185)	(47,539)
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 160,364</u>	<u>\$ 118,134</u>	<u>\$ 278,498</u>

City of Montrose

Fiduciary Funds

STATEMENT OF FIDUCIARY NET ASSETS

June 30, 2005

	Current Tax Collection	Delinquent Tax Collection	Total
ASSETS			
Cash	<u>\$ 18,665</u>	<u>\$ 3,806</u>	<u>\$ 22,471</u>
LIABILITIES			
Due to other governmental units	<u>\$ 18,665</u>	<u>\$ 3,806</u>	<u>\$ 22,471</u>

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The City of Montrose is located in Genesee County, Michigan and has a population of approximately 1,811. The City of Montrose operates with a Council form of government and provides services to its residents in many areas including general government, highways and streets, human services, and utilities services.

The City has six (6) City Council members who are elected at large for overlapping four (4) year terms and a Mayor elected at large for a two (2) year term. The Council appoints the City Manager, Treasurer, Clerk, and Assessor.

The financial statements of the City have been prepared in accordance with generally accepted accounting principles (GAAP) as applied to City governments. The Governmental Accounting Standards Board is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The City's more significant accounting policies are described below.

1. Reporting Entity

As required by accounting principles generally accepted in the United States of America; GASB Statement 14, *The Financial Reporting Entity*; and *Statement on Michigan Governmental Accounting and Auditing No. 5*, these financial statements present the financial activities of the City of Montrose (primary government) and its component unit, an entity for which the government is considered to be financially accountable. The discretely presented component unit is reported in a separate column in the government-wide financial statements to emphasize that it is legally separate from the City.

2. Discretely Presented Component Unit

The component unit columns in the financial statements include the financial data of the City's component unit (Downtown Development Authority). The governing body of the Downtown Development Authority is appointed by the City Council, the Authority's budget is subject to the approval of the City Council and the City temporarily relinquishes part of its tax base to the Authority (tax increment revenues).

3. Basis of Presentation

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The statement of net assets and the statement of activities (the government-wide statements) present information for the primary government and its component unit as a whole. All non-fiduciary activities of the primary government are included (i.e., fiduciary fund activities are not included in the government-wide statements). For the most part, interfund activity has been eliminated in the preparation of these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities presents the direct functional expenses of the primary government and its component unit and the program revenues that support them. Direct expenses are specifically associated with a service, program, or department and are therefore clearly identifiable to a particular function. Program revenues are associated with specific functions and include charges to recipients of goods or services and grants and contributions that are restricted to meeting the operational or capital requirements of that function. Revenues that are not required to be presented as program revenues are general revenues. This includes all taxes, interest, and unrestricted State revenue sharing payments and other general revenues and shows how governmental functions are either self-financing or supported by general revenues.

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

3. Basis of Presentation - continued

FUND FINANCIAL STATEMENTS

The fund financial statements present the City's individual major funds and aggregated nonmajor funds. Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

The major funds of the City are:

- a. The General Fund is the City's primary operating fund. It accounts for all financial resources of the general government except for those that are required to be accounted for in another fund.
- b. The Major Street Fund is used to account for the financial resources that are used for repairs and maintenance of the City's major streets.
- c. The Local Street Fund is used to account for the financial resources that are used for repairs and maintenance of the City's local streets.
- d. The Capital Projects Fund accounts for resources, which have the purpose of making capital improvements to the City.
- e. The Sewer System Fund accounts for resources generated by providing sewer services to residents of the City; the costs (expenses, including depreciation) are financed or recovered primarily through user charges.
- f. The Water System Fund accounts for resources generated by providing water services to residents of the City; the costs (expenses, including depreciation) are financed or recovered primarily through user charges.

4. Measurement Focus

The government-wide and proprietary fund financial statements are presented using the economic resources measurement focus, similar to that used by business enterprises or not-for-profit organizations. Because another measurement focus is used in the governmental fund financial statements, reconciliations to the government-wide statements are provided that explain the differences in detail.

All governmental funds are presented using the current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

There is no measurement focus for the fiduciary agency fund since assets equal liabilities.

5. Basis of Accounting

Basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurement made, regardless of the measurement focus applied.

All governmental funds are accounted for using the modified accrual basis of accounting. Under this method, revenues are recognized when they become susceptible to accrual (when they become both "measurable" and "available to finance expenditures of the current period"). The length of time used for "available" for purposes of revenue recognition in the governmental fund financial statements is 60 days.

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

5. Basis of Accounting - continued

Revenues that are considered measurable but not available are recorded as a receivable and deferred revenue. Significant revenues susceptible to accrual are special assessments and certain intergovernmental revenues. Expenditures are generally recognized under the modified accrual basis of accounting when the related fund liability is incurred, except for interest on long-term debt which is recorded when due.

All proprietary funds are accounted for using the accrual basis of accounting. Their revenues are recognized when they are earned, and their expenses are recognized when they are incurred.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the Enterprise Funds are charges to customers for sales and services. Operating expenses for enterprise funds include the costs of sales and services, administrative expenses, and other costs of running the activity. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. If/when both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed.

6. Budgets and Budgetary Accounting

The General and Special Revenue Funds' budgets are prepared on a basis consistent with the modified accrual basis used to reflect actual results. The City employs the following procedures in establishing its budgetary data.

- a. Prior to April 15, the City Manager submits to the City Council a proposed operating budget for the fiscal year beginning the following July 1. The operating budget includes proposed expenditures and the means of financing them.
- b. A Public Hearing is conducted to obtain taxpayers' comments.
- c. Prior to the second week of May, the budget is legally adopted by appropriating the funds necessary to operate.
- d. The budget is legally adopted at the functional level for the General Fund and Special Revenue Funds; however they are maintained at the account level for control purposes.
- e. The City does not employ encumbrance accounting as an extension of formal budgetary integration in the governmental funds. Appropriations unused at June 30 are not carried forward to the following fiscal year.
- f. Any revisions to the budget must be approved by the City Council.

7. Cash and Cash Equivalents

Cash and cash equivalents consist of various savings and money market checking accounts and pooled investment accounts. The cash and cash equivalents are recorded at cost, which approximates market value.

8. Restricted Cash

A portion of the cash and cash equivalents of the Water Fund is classified as restricted cash because its use is limited. The Water Fund's restrictions are due to bond resolution requirements to maintain certain balances in separate accounts for debt service and general purpose reserves, and also for the amount of customer deposits held at June 30, 2005.

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

9. Property Tax

The City of Montrose bills and collects its own property taxes and also taxes for other governmental units. The City's property tax revenue recognition policy and related tax calendar disclosures are highlighted in the following paragraph.

Property taxes are levied by the City of Montrose on July 1 and December 1 and are payable without penalty through September 30 and February 28, respectively. The July 1 levy is composed of the City's millage, special assessments, and the school taxes. The December 1 levy is composed of county, school taxes, and special assessments. All real property taxes not paid to the City by March 1 are turned over to the Genesee County Treasurer for collection. The Genesee County Treasurer purchases the receivables of all taxing districts on any delinquent real property taxes. Delinquent personal property taxes are retained by the City for subsequent collection. Collections and remittances of all taxes are accounted for in the Current Tax Collections Agency Fund. City property tax revenues are recognized as revenues in the fiscal year levied.

The City is permitted to levy taxes up to 20 mills (\$20 per \$1,000 of taxable valuation) for general governmental services. For the year ended June 30, 2005, the City levied 17.7501 mills per \$1,000 of assessed valuation for general governmental services. The total Taxable Value for the 2004 levy for property within the City was \$23,151,021.

10. Interfund Transactions

During the course of normal operations, the City has numerous transactions between funds, including expenditures and transfers of resources to provide services, construct assets, and service debt. The accompanying financial statements generally reflect such transactions as transfers. Transfers between governmental and proprietary funds are netted as part of the reconciliation to the government-wide financial statements.

11. Compensated Absences

City employees are granted sick and vacation leave in varying amounts. In the event of termination, an employee is paid for accumulated sick and vacation time. All employees with accumulated unused sick and vacation time pay at June 30, 2005 were vested and the total due to them, along with the related payroll taxes, is recorded in the governmental-wide financial statements. For proprietary funds, the cost is recorded as a fund liability when earned.

12. Capital Assets

Capital assets include land, buildings, equipment, and vehicles and are recorded (net of accumulated depreciation, if applicable) in the government-wide financial statements under the governmental activities and component unit columns. Capital assets are those with an initial individual cost of \$1,500 or more and an estimated useful life of more than one year. Capital assets are not recorded in the governmental funds. Instead, capital acquisition and construction are reflected as expenditures in governmental funds, and the related assets are reported in the government-wide financial statements. All purchased capital assets are valued at cost where historical records are available and at an estimated historical cost where no historical records exist. Donated capital assets are valued at their estimated fair market value on the date received.



## NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED****12. Capital Assets - continued**

GASB Statement No. 34 requires major networks and major subsystems of infrastructure assets acquired, donated, constructed, or substantially rehabilitated since fiscal years ending after June 30, 1980, be inventoried and capitalized by the fourth anniversary of the mandated date of adoption of the other provisions of GASB Statement No. 34. The City of Montrose has capitalized infrastructure as required since implementing GASB Statement No. 34, and has reported the infrastructure in the Statement of Net Assets. The City of Montrose will retroactively capitalize the major infrastructure assets on or before June 30, 2008, as permitted by GASB Statement No. 34.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Depreciation is computed using the straight-line method over the following useful lives:

Sewer and Water systems and improvements	10 - 50 years
Equipment and machinery	3 - 12 years
Buildings	25 years
Vehicles	10 years
Infrastructure	20 - 50 years

**13. Long-term Liabilities**

Long-term debt and other long-term obligations are recognized as a liability in the government-wide financial statements and proprietary fund types when incurred. The portion of those liabilities expected to be paid within the next year is a current liability with the remaining amounts shown as long-term.

Long-term debt is recognized as a liability of a governmental fund when due. For other long-term obligations, only that portion expected to be financed from expendable available financial resources is reported as a fund liability of a governmental fund.

**14. Comparative Data**

Comparative data for the prior year has not been presented in all funds in the accompanying financial statements since their inclusion would make the financial statements unduly complex and difficult to read.

**NOTE B: CASH AND CASH EQUIVALENTS**

In accordance with Michigan Compiled Laws, the City is authorized to invest in the following investment vehicles:

1. Bonds, securities, and other obligations of the United States or an agency or instrumentality of the United States.
2. Certificates of deposit, savings accounts, deposit accounts, or depository receipts of a State or nationally chartered bank or a State or Federally chartered savings and loan association, savings bank, or credit union whose deposits are insured by an agency of the United States government and which maintains a principal office or branch office located in this State under the laws of the State or the United States, but only if the bank, savings and loan association, savings bank, or credit union is eligible to be a depository of surplus funds belong to the State under Section 5 or 6 of Act No. 105 of the Public Acts of 1855, as amended, being Section 21.145 and 21.146 of Michigan Compiled Laws.
3. Commercial paper rated at the time of purchase within the three (3) highest classifications established by not less than two (2) standard rating services and which matures not more than 270 days after the date of purchase.

## NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE B: CASH AND CASH EQUIVALENTS - CONTINUED**

4. The United States government or federal agency obligations repurchase agreements.
5. Bankers acceptances of United States banks.
6. Mutual funds composed of investment vehicles, which are legal for direct investment by local units of government in Michigan.

Federal Deposit Insurance Corporation (FDIC) regulations provide that deposits of governmental units are to be separately insured for the amount of \$100,000 for deposits in an insured bank for savings deposits and \$100,000 for demand deposits. Furthermore, if specific deposits are regulated by statute or bond indenture, these specific deposits are to be separately insured for the amount of \$100,000. Michigan Compiled Laws allow for collateralization of government deposits, if the assets for pledging are acceptable to the State Treasurer under Section 3 of 1855 PA 105, MCL 21.143, to secure deposits of State surplus funds, securities issued by the Federal Loan Mortgage Corporation, Federal National Mortgage Association, or Government National Mortgage Association.

Deposits

As of June 30, 2005, the carrying amounts and bank balances for each type of bank account are as follows:

<u>Account Type</u>	<u>Carrying Amount</u>	<u>Bank Balance</u>
PRIMARY GOVERNMENT		
Regular checking	\$ 71,842	\$ 34,375
Money market	<u>1,666,850</u>	<u>1,666,850</u>
Total Primary Government	1,738,692	1,701,225
COMPONENT UNIT		
Money market	67,088	67,088
FIDUCIARY FUNDS		
Regular checking	300	303
Money market	<u>22,171</u>	<u>123,451</u>
Total Fiduciary Funds	<u>22,471</u>	<u>123,751</u>
TOTAL REPORTING UNIT	<u>\$ 1,828,251</u>	<u>\$ 1,892,064</u>

Deposits of the City are at federally insured banks located in the State of Michigan with all accounts maintained in the name of the City. As of June 30, 2005, the City accounts were insured by the FDIC for \$136,756, and the amount of \$1,755,308 was uninsured and uncollateralized.

Due to significantly higher cash flow at certain periods during the year, the amount the City held as cash and cash equivalents increased significantly. As a result, the amount of uninsured and uncollateralized cash and cash equivalents were substantially higher at these peak periods than at year-end.

## NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE B: CASH AND CASH EQUIVALENTS - CONTINUED**Investments

As of June 30, 2005, the carrying amounts and market values for each type of investment as reported in the cash and cash equivalents captions on the basic financial statements are as follows:

<u>INVESTMENT TYPE</u>	<u>Carrying Amount</u>	<u>Bank Balance</u>	<u>Weighted Average Maturity (years)</u>
PRIMARY GOVERNMENT			
Uncategorized pooled investment funds			
MBIA	\$ 271,237	\$ 271,237	29 days
Bank One	333,600	333,600	39 days
Public Funds Investment Trust	<u>534,676</u>	<u>534,676</u>	< 60 days
	<u>\$ 1,139,773</u>	<u>\$ 1,139,773</u>	

Credit risk

State law limits investments in certain types of investments to a prime or better rating issued by nationally recognized statistical rating organizations (NRSRO's). As of June 30, 2005, the Public Funds Investment Trust was rated AAA by Standard and Poor's. The Bank One investment was rated AAA by Moody's. The MBIA - Michigan Class investment is not rated.

Interest rate risk

The City has not adopted a policy that indicates how the City will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates, by limiting the weighted average maturity of its investment portfolio to less than a given period of time.

Concentration of credit risk

The City has not adopted a policy that indicates how the City will minimize concentration of credit risk, which is the risk of loss attributed to the magnitude of the City's investment in a single issuer, by diversifying the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimized.

Custodial credit risk

The City has not adopted a policy that indicates how the City will minimize custodial credit risk, which is the risk that in the event of the failure of the counterparty, the City will not be able to recover the value of its investments of collateral securities that are in possession of an outside party.

The cash and cash equivalents and investments referred to above have been reported in the cash and cash equivalents caption on the basic financial statements, based upon criteria disclosed in Note A. The following summarizes the categorization of these amounts as of June 30, 2005:

	<u>Primary Government</u>	<u>Component Unit</u>	<u>Fiduciary Funds</u>	<u>Reporting Entity</u>
Cash and cash equivalents	<u>\$ 2,878,465</u>	<u>\$ 67,088</u>	<u>\$ 22,471</u>	<u>\$ 2,968,024</u>

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE C: INTERFUND TRANSFERS**

Permanent reallocation of resources between funds of the reporting entity is classified as interfund transfers. For the purpose of the statement of activities, all interfund transfers between individual governmental funds have been eliminated.

Transfers to General Fund from:	
Nonmajor governmental funds	\$ 385
Sewer System Fund	<u>55,600</u>
	55,985
Transfers to Local Street Fund from:	
Major Street Fund	19,676
Sewer System Fund	<u>430,000</u>
	449,676
Transfers to nonmajor governmental funds from:	
Capital Projects Fund	<u>2,077</u>
	<u>\$ 507,738</u>

**NOTE D: CAPITAL ASSETS**

Capital asset activity for the year ended June 30, 2005 was as follows:

**PRIMARY GOVERNMENT**

	Restated Balance <u>July 1, 2004</u>	<u>Additions</u>	<u>Deletions</u>	Balance <u>June 30, 2005</u>
<b>Governmental activities</b>				
Capital assets not being depreciated				
Construction in progress	\$ 10,000	\$ 78,994	\$ -	\$ 88,994
Land	<u>99,000</u>	<u>-</u>	<u>-</u>	<u>99,000</u>
Total capital assets not being depreciated	109,000	78,994	-0-	187,994
Capital assets being depreciated				
Buildings	68,800	-	-	68,800
Furniture and equipment	38,000	74,055	-	112,055
Vehicles	256,500	-	-	256,500
Infrastructure	<u>148,444</u>	<u>288,956</u>	<u>-</u>	<u>437,400</u>
Total capital assets, being depreciated	511,744	363,011	-0-	874,755
Less accumulated depreciation for:				
Buildings	( 68,800 )	-	-	( 68,800 )
Furniture and equipment	( 28,417 )	( 3,639 )	-	( 32,056 )
Vehicles	( 215,643 )	( 8,643 )	-	( 224,286 )
Infrastructure	<u>( 6,596 )</u>	<u>( 6,679 )</u>	<u>-</u>	<u>( 13,275 )</u>
Total accumulated depreciation	<u>( 319,456 )</u>	<u>( 18,961 )</u>	<u>-0-</u>	<u>( 338,417 )</u>
Net capital assets being depreciated	<u>192,288</u>	<u>344,050</u>	<u>-0-</u>	<u>536,338</u>
Capital assets, net	<u>\$ 301,288</u>	<u>\$ 423,044</u>	<u>\$ -0-</u>	<u>\$ 724,332</u>

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE D: CAPITAL ASSETS - CONTINUED**

PRIMARY GOVERNMENT - CONTINUED

Depreciation expense was charged to activities of the following governmental activities:

General government	\$ 3,639
Public works	<u>15,322</u>
Total depreciation expense	<u>\$ 18,961</u>

	Balance July 1, 2004	Additions	Deletions	Balance June 30, 2005
<b>Business-type activities</b>				
<b>(Sewer system)</b>				
Capital assets not being depreciated				
Land	\$ 50,620	\$ -	\$ -	\$ 50,620
Construction in progress	<u>-</u>	<u>5,468</u>	<u>-</u>	<u>5,468</u>
Total capital assets not being depreciated	50,620	5,468	-0-	56,088
Capital assets being depreciated				
Sewer system	2,320,124	-	-	2,320,124
Equipment	<u>6,921</u>	<u>-</u>	<u>-</u>	<u>6,921</u>
Total capital assets, being depreciated	2,327,045	-0-	-0-	2,327,045
Less accumulated depreciation for:				
Sewer system	( 1,554,778 )	( 57,902 )	-	( 1,612,680 )
Equipment	<u>( 6,921 )</u>	<u>-</u>	<u>-</u>	<u>( 6,921 )</u>
Total accumulated depreciation	<u>( 1,561,699 )</u>	<u>( 57,902 )</u>	<u>-0-</u>	<u>( 1,619,601 )</u>
Net capital assets being depreciated	<u>765,346</u>	<u>( 57,902 )</u>	<u>-0-</u>	<u>707,444</u>
Capital assets, net	<u>\$ 815,966</u>	<u>\$ ( 52,434 )</u>	<u>\$ -0-</u>	<u>\$ 763,532</u>
<b>Business-type activities</b>				
<b>(Water system)</b>				
Capital assets not being depreciated				
Construction in progress	\$ -	\$ 6,296	\$ -	\$ 6,296
Capital assets being depreciated				
Water system	1,924,281	-	-	1,924,281
Equipment	<u>6,922</u>	<u>-</u>	<u>-</u>	<u>6,922</u>
Total capital assets, being depreciated	1,931,203	-0-	-0-	1,931,203
Less accumulated depreciation for:				
Water system	( 745,952 )	( 38,863 )	-	( 784,815 )
Equipment	<u>( 6,922 )</u>	<u>-</u>	<u>-</u>	<u>( 6,922 )</u>
Total accumulated depreciation	<u>( 752,874 )</u>	<u>( 38,863 )</u>	<u>-0-</u>	<u>( 791,737 )</u>
Net capital assets being depreciated	<u>1,178,329</u>	<u>( 38,863 )</u>	<u>-0-</u>	<u>1,139,466</u>
Capital assets, net	<u>\$ 1,178,329</u>	<u>\$ ( 32,567 )</u>	<u>\$ -0-</u>	<u>\$ 1,145,762</u>

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE D: CAPITAL ASSETS - CONTINUED**

COMPONENT UNIT

	Balance July 1, 2004	Additions	Deletions	Balance June 30, 2005
<b>Downtown Development Authority</b>				
Capital assets not being depreciated				
Land	\$ 38,000	\$ -	\$ -	\$ 38,000
Capital assets being depreciated				
Infrastructure	98,223	-	-	98,223
Less accumulated depreciation for:				
Infrastructure	( 4,911 )	( 4,911 )	-	( 9,822 )
Net capital assets being depreciated	93,312	( 4,911 )	-0-	88,401
Capital assets, net	<u>\$ 131,312</u>	<u>\$( 4,911 )</u>	<u>\$ -0-</u>	<u>\$ 126,401</u>

**NOTE E: LONG-TERM DEBT**

The following is a summary of changes in long-term debt (including current portion) of the City for the year ended June 30, 2005:

	Balance July 1, 2004	Additions	Deletions	Balance June 30, 2005	Amounts Due Within One Year
<b>PRIMARY GOVERNMENT</b>					
Governmental activities					
2005 General Obligation Bonds	\$ -	\$ 750,000	\$ -	\$ 750,000	\$ 35,000
Installment loan	-	74,055	-	74,055	11,438
Accumulated sick/vacation	2,046	2,434	-	4,480	2,863
	2,046	826,489	-0-	828,535	49,301
Business-type activities					
Enterprise Funds					
Water System Fund					
1981 Water Revenue Bonds	815,000	-	35,000	780,000	35,000
Accumulated sick/vacation	5,598	-	1,442	4,156	401
	820,598	-0-	36,442	784,156	35,401
Sewer System Fund					
Accumulated sick/vacation	5,598	-	1,442	4,156	401
	826,196	-0-	37,884	788,312	35,802
<b>TOTAL PRIMARY GOVERNMENT</b>	<u>\$ 828,242</u>	<u>\$ 826,489</u>	<u>\$ 37,884</u>	<u>\$ 1,616,847</u>	<u>\$ 85,103</u>

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE E: LONG-TERM DEBT - CONTINUED**

Significant details regarding outstanding long-term debt (including current portion) are presented below:

**PRIMARY GOVERNMENT**

Accrued Sick/Vacation

Individual employees have vested rights upon termination of employment to receive payments for unused vacation and sick leave. The dollar amounts of these vested rights including related payroll taxes, which have been accrued in the financial statements either on the respective fund Balance Sheet or the governmental-wide financial statements, amounted to approximately \$12,792 at June 30, 2005. Of this amount, \$8,312 is recorded as a liability within the Enterprise funds, in accordance with criteria disclosed in Note A.

General Obligation Bonds

\$750,000 Limited Tax General Obligation Bonds, dated May 1, 2005, due in annual installments ranging from \$35,000 to \$65,000 through May 1, 2020, with interest ranging from 4.00 to 5.00 percent, payable semi-annually. \$ 750,000

Revenue Bonds

\$940,000 1981 Water Revenue Bonds, due in annual installments ranging from \$35,000 to \$70,000 through April 1, 2021 with interest at 5.00 percent, payable semi-annually. \$ 780,000

Installment Loan Payable

\$74,055 Installment Loan Payable for a backhoe, dated May 6, 2005, due in monthly payments of \$2,214, with interest of 4.60 percent. \$ 74,055

The annual requirements to pay the debt principal and interest outstanding for the bonds are as follows:

Year Ending June 30,	<u>General Obligation</u>		<u>Revenue Bonds</u>		<u>Installment Loans</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2006	\$ 35,000	\$ 32,502	\$ 35,000	\$ 38,000	\$ 23,396	\$ 3,172
2007	40,000	30,753	35,000	36,250	24,748	1,820
2008	40,000	28,752	40,000	34,500	25,911	640
2009	40,000	26,753	40,000	32,500	-	-
2010	45,000	24,752	40,000	30,500	-	-
2011-2015	245,000	96,163	245,000	119,250	-	-
2016-2020	305,000	40,700	320,000	50,500	-	-
2021	-	-	25,000	1,250	-	-
	<u>\$ 750,000</u>	<u>\$ 280,375</u>	<u>\$ 780,000</u>	<u>\$ 342,750</u>	<u>\$ 74,055</u>	<u>\$ 5,632</u>

**NOTE F: EXCESS OF EXPENDITURES OVER APPROPRIATIONS**

Michigan Public Act 621 of 1978, Sections 18 and 19, as amended, provides that a local governmental unit not incur expenditures in excess of the amounts appropriated and adopt budgets for the General Fund and all Special Revenue Funds.

## NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE F: EXCESS OF EXPENDITURES OVER APPROPRIATIONS - CONTINUED**

In the required supplementary information, the City's budgeted expenditures for the General Fund and major Special Revenue Funds have been shown at the functional classification level. The approved budgets of the City have been adopted at the functional level for the General Fund.

During the year ended June 30, 2005, the City incurred expenditures in the General Fund in excess of the amounts appropriated as follows:

	<u>Amounts Appropriated</u>	<u>Amounts Expended</u>	<u>Variance</u>
General Fund			
Public works			
Department of public works	\$ 72,513	\$ 130,083	\$ 57,570

The budget variance noted above was caused by an audit adjustment to appropriately reflect the financed purchase of a backhoe as an expenditure of the current fiscal year.

**NOTE G: RISK MANAGEMENT**

The City participates in a pool, the Michigan Township Participating Plan with other municipalities for various risks of loss including employer's liability, errors and omissions, and property and casualty losses. The pool is organized under Public Act 138 of 1982, as amended. The City has no liability for additional assessments based on the claims filed against the pool nor do they have any right to dividends.

The City also participates in a pool, the Michigan Municipal Workers' Compensation Fund, with other municipalities for workers' compensation losses. The pool is organized under Public Act 317 of 1969, as amended. The City has no liability for additional assessments based on the claims filed against the pool nor do they have any right to dividends.

**NOTE H: RETIREMENT PLAN**Plan Description

The City participates in the Michigan Municipal Employees Retirement System, an agent multiple-employer defined benefit pension plan that covers all eligible full-time employees of the City. The system provides retirement, disability, and death benefits to plan members and their beneficiaries.

Funding Policy

The Michigan Municipal Employees Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the system. That report may be obtained by writing to the System at 1134 Municipal Way, Lansing, Michigan 48917.

The obligation to contribute to and maintain the system for these employees was established by the City Council and by negotiation with the City's collective bargaining units. The plan requires no contribution from the employees.



## NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE H: RETIREMENT PLAN - CONTINUED**Annual Pension Cost

For year ended June 30, 2005, the City's annual pension cost of \$34,587 for the plan was equal to the City's required and actual contribution. The estimated annual required contribution was determined as part of an actuarial valuation at December 31, 2002, using the entry actual age cost method. Actual required contributions are based on actual reported monthly payroll. Significant actuarial assumptions used include a (a) 8.00 percent investment rate of return (b) projected salary increases of 4.5 percent per year compounded annually, attributable to inflation (c) additional salary increases ranging from 0% to 4.16% per year depending on age, seniority and merit, and (d) assumption benefits will not increase after retirement.

The actuarial value of assets was determined using techniques that smooth the effects of short term volatility over a four (4) year period. The unfunded actuarial liability is being amortized as a level percentage of payroll over a period of thirty years.

Three (3) year trend information

	Year Ended December 31,		
	<u>2002</u>	<u>2003</u>	<u>2004</u>
Actuarial value of assets	\$ 242,308	\$ 282,739	\$ 334,075
Actuarial accrued liability (AAL) (entry age)	613,443	624,005	744,335
Unfunded AAL	371,135	341,266	410,260
Funded ratio	39 %	45 %	45 %
Covered payroll	146,129	153,392	125,454
UAAL as a percentage of covered payroll	254 %	222 %	327 %

  

	Year Ended June 30,		
	<u>2003</u>	<u>2004</u>	<u>2005</u>
Annual pension cost	\$ 30,244	\$ 42,393	\$ 34,587
Percentage of APC contributed	100 %	100 %	100 %
Net pension obligation	-	-	-

This trend information was obtained from the most recently issued actuarial reports.

**NOTE I: BUILDING CODE FINANCIAL INFORMATION**

The City elected to report the financial activities of the building and code enforcement department in the General Fund. The following is the required information as it relates to this department for the year ended June 30, 2005:

REVENUES	
Building permits	\$ 7,778
EXPENDITURES	
Contracted services	<u>9,244</u>
EXCESS OF REVENUES (UNDER) EXPENDITURES	
	<u>\$( 1,466 )</u>

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

**NOTE J: PRIOR PERIOD ADJUSTMENTS**

The following prior period adjustments were made during the current period, which were the result of corrections of accounting errors. These adjustments were reported as changes to beginning net assets and fund equity, respectively. The effect on operations and other affected balances for the current year and prior period are as follows:

	June 30, <u>2005</u>	<u>2004</u>	<u>Description</u>
<b>PRIMARY GOVERNMENT</b>			
Governmental activities			
Capital assets, net	\$ -	\$ 7,857	Correct understated capital
Net assets - beginning	7,857	-	assets, net of accumulated depreciation
<b>COMPONENT UNIT</b>			
Downtown Development Authority			
Due to other governmental units	-	( 22,395 )	Correct overstated due to other
Revenues over expenditures/expenses	-	22,395	governmental units
Fund balance/net assets - beginning	22,395	-	

**NOTE K: FUND EQUITY RESERVES AND DESIGNATIONS**

Reserved fund balance is used to earmark a portion of fund balance to indicate that it is not appropriate for expenditure or has been legally segregated for a specific future use. Designated fund equity indicates that portion of fund balance or net assets with the City has set aside for specific purposes. These reserves and designations are recorded at the fund level to indicate management plans for these funds.

The following is the fund balance reserve as of June 30, 2005:

Debt Service Funds	
Non-voted Bonds Fund	
Reserved for debt service	<u>\$ 2,078</u>

The following is the fund balance designation as of June 30, 2005:

Capital Project Fund	
Designated for capital expenditures	<u>\$ 743,107</u>

## **REQUIRED SUPPLEMENTARY INFORMATION**

## City of Montrose

## General Fund

## BUDGETARY COMPARISON SCHEDULE

Year Ended June 30, 2005

	Budgeted Amounts			Variance with Final Budget Positive (Negative)
	Original	Final	Actual	
REVENUES				
Taxes				
Property taxes	\$ 336,848	\$ 380,066	\$ 381,719	\$ 1,653
Fees in lieu of taxes	5,540	14,566	14,566	-0-
Penalties and interest	5,551	6,297	6,298	1
Administration fees	3,314	6,525	6,525	-0-
Total taxes	351,253	407,454	409,108	1,654
Licenses and permits				
Cable television license	11,875	11,838	11,838	-0-
City licenses and permits	13,759	9,937	9,938	1
Total licenses and permits	25,634	21,775	21,776	1
Intergovernmental				
State - sales tax	237,850	194,393	194,393	-0-
Federal - CDBG	27,343	-	-	-0-
Total intergovernmental	265,193	194,393	194,393	-0-
Charges for services				
Solid waste	57,907	51,948	51,948	-0-
Special assessments	-	1,653	1,653	
Other	-	350	351	1
Total charges for services	57,907	53,951	53,952	1
Fines and forfeits				
Parking	5,192	6,773	6,773	-0-
Interest and rents				
Interest	3,013	3,627	3,629	2
Rents	29,889	36,127	36,128	1
Total interest and rents	32,902	39,754	39,757	3
Other	36,401	4,006	2,689	(1,317)
TOTAL REVENUES	774,482	728,106	728,448	342
EXPENDITURES				
General government				
Council, boards, and commissions	37,268	38,055	37,378	677
Mayor	11,900	3,076	2,574	502
City Manager	60,930	63,068	58,438	4,630

## City of Montrose

## General Fund

## BUDGETARY COMPARISON SCHEDULE - CONTINUED

Year Ended June 30, 2005

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
EXPENDITURES - CONTINUED				
General government - continued				
Elections	\$ 5,520	\$ 2,862	\$ 2,856	\$ 6
Assessor	9,525	11,949	11,128	821
Clerk	75,732	79,622	73,275	6,347
Board of Review	535	1,154	912	242
Treasurer	49,393	60,863	58,419	2,444
City Hall and grounds	68,995	67,626	63,701	3,925
Other	6,800	9,900	9,900	-0-
Total general government	326,598	338,175	318,581	19,594
Public safety				
Police services	182,474	213,306	213,303	3
Fire services	46,667	46,935	46,930	5
Building and code enforcement	10,000	9,480	9,244	236
Total public safety	239,141	269,721	269,477	244
Public works				
Department of public works	67,198	72,513	130,083	(57,570)
Street lighting	20,706	21,606	21,573	33
Sanitation	57,907	51,948	48,016	3,932
Total public works	145,811	146,067	199,672	(53,605)
Community and economic development	8,308	6,695	6,346	349
Recreation and cultural				
Senior citizens center	-	1,749	1,177	572
Parks and recreation	34,124	11,379	10,313	1,066
Library	4,000	4,000	3,900	100
Total recreation and cultural	38,124	17,128	15,390	1,738
TOTAL EXPENDITURES	757,982	777,786	809,466	(31,680)
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	16,500	(49,680)	(81,018)	(31,338)

## City of Montrose

## General Fund

## BUDGETARY COMPARISON SCHEDULE - CONTINUED

Year Ended June 30, 2005

	<u>Budgeted Amounts</u>		<u>Actual</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
OTHER FINANCING SOURCES				
Loan proceeds	\$ -	\$ -	\$ 74,055	\$ 74,055
Transfer in	-	55,985	55,985	-0-
TOTAL OTHER FINANCING SOURCES	<u>-0-</u>	<u>55,985</u>	<u>130,040</u>	<u>74,055</u>
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES	16,500	6,305	49,022	42,717
Fund balances, beginning of year	<u>149,963</u>	<u>149,963</u>	<u>149,963</u>	<u>-0-</u>
Fund balances, end of year	<u>\$ 166,463</u>	<u>\$ 156,268</u>	<u>\$ 198,985</u>	<u>\$ 42,717</u>

## City of Montrose

## Major Street

## BUDGETARY COMPARISON SCHEDULE

Year Ended June 30, 2005

	<u>Budgeted Amounts</u>		<u>Actual</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
REVENUES				
Intergovernmental	\$ 80,585	\$ 89,577	\$ 89,576	\$ (1)
Interest	980	980	1,762	782
Other	7,430	7,430	7,859	429
TOTAL REVENUES	88,995	97,987	99,197	1,210
EXPENDITURES				
Current				
Public works	56,213	60,067	50,797	9,270
EXCESS OF REVENUES OVER EXPENDITURES	32,782	37,920	48,400	10,480
OTHER FINANCING USES				
Transfers out	(18,750)	(19,676)	(19,676)	-0-
EXCESS OF REVENUES OVER EXPENDITURES AND OTHER FINANCING USES	14,032	18,244	28,724	10,480
Fund balance, beginning of year	150,164	150,164	150,164	-0-
Fund balance, end of year	<u>\$ 164,196</u>	<u>\$ 168,408</u>	<u>\$ 178,888</u>	<u>\$ 10,480</u>

City of Montrose

Local Street

BUDGETARY COMPARISON SCHEDULE

Year Ended June 30, 2005

	Budgeted Amounts			Variance with Final Budget Positive (Negative)
	Original	Final	Actual	
REVENUES				
Intergovernmental	\$ 56,343	\$ 56,343	\$ 56,876	\$ 533
Interest	2,967	750	1,126	376
Other	25,526	44,526	45,553	1,027
TOTAL REVENUES	84,836	101,619	103,555	1,936
EXPENDITURES				
Current				
Public works	426,015	443,422	436,123	7,299
EXCESS OF REVENUES (UNDER) EXPENDITURES	(341,179)	(341,803)	(332,568)	9,235
OTHER FINANCING SOURCES				
Transfers in	448,750	449,676	449,676	-0-
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES	107,571	107,873	117,108	9,235
Fund (deficit), beginning of year	(66,934)	(66,934)	(66,934)	-0-
Fund balance, end of year	\$ 40,637	\$ 40,939	\$ 50,174	\$ 9,235



## **OTHER SUPPLEMENTARY INFORMATION**

City of Montrose  
Nonmajor Governmental Funds  
COMBINING BALANCE SHEET  
June 30, 2005

	Special Revenue	Debt Service		Total Nonmajor Governmental Funds
	Depot Fund	Voted Bonds	Non-Voted Bonds	
ASSETS				
Cash and cash equivalents	<u>\$ 9,968</u>	<u>\$ -</u>	<u>\$ 2,078</u>	<u>\$ 12,046</u>
LIABILITIES AND FUND BALANCES				
LIABILITIES				
Accounts payable	\$ 1,500	\$ -	\$ -	\$ 1,500
FUND BALANCES				
Reserved for debt service	-	-	2,078	2,078
Unreserved - undesignated	<u>8,468</u>	<u>-</u>	<u>-</u>	<u>8,468</u>
TOTAL FUND BALANCES	<u>8,468</u>	<u>-</u>	<u>2,078</u>	<u>10,546</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 9,968</u>	<u>\$ -0-</u>	<u>\$ 2,078</u>	<u>\$ 12,046</u>

City of Montrose

Nonmajor Governmental Funds

COMBINING STATEMENT OF REVENUES, EXPENDITURES,  
AND CHANGES IN FUND BALANCES

Year Ended June 30, 2005

	Special Revenue Depot Fund	Debt Service		Total Nonmajor Governmental Funds
		Voted Bonds	Non-Voted Bonds	
REVENUES				
Interest	\$ 106	\$ 48	\$ 1	\$ 155
Other	23,115	-	-	23,115
TOTAL REVENUES	23,221	48	1	23,270
EXPENDITURES				
Current				
Community and economic development	36,020	-	-	36,020
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	(12,799)	48	1	(12,750)
OTHER FINANCING SOURCES (USES)				
Transfer in	-	-	2,077	2,077
Transfer out	-	(385)	-	(385)
TOTAL OTHER FINANCING SOURCES (USES)	-0-	(385)	2,077	1,692
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING USES	(12,799)	(337)	2,078	(11,058)
Fund balance, beginning of year	21,267	337	-	21,604
Fund balance, end of year	\$ 8,468	\$ -0-	\$ 2,078	\$ 10,546

City of Montrose  
Component Unit Fund  
GOVERNMENTAL FUND BALANCE SHEET  
June 30, 2005

	<u>Special Revenue</u>
	<u>Downtown Development Authority</u>
ASSETS	
Cash	<u>\$          67,088</u>
LIABILITIES AND FUND BALANCE	
LIABILITIES	
Accounts payable	\$          275
FUND BALANCE	
Unreserved - undesignated	<u>66,813</u>
TOTAL LIABILITIES AND FUND BALANCE	<u>\$          67,088</u>

City of Montrose

Component Unit Fund

RECONCILIATION OF THE GOVERNMENTAL FUND BALANCE SHEET  
TO THE STATEMENT OF NET ASSETS - DOWNTOWN DEVELOPMENT AUTHORITY

June 30, 2005

**Fund balance - governmental fund** \$ 66,813

Amounts reported for the governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources  
and therefore are not reported as assets in the governmental funds.

The cost of capital assets is	\$ 136,223
Accumulated depreciation is	<u>(9,822)</u>

Capital assets, net	<u>126,401</u>
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<b>Net assets of governmental activities</b>	<u><u>\$ 193,214</u></u>
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City of Montrose

Component Unit Fund

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE

Year Ended June 30, 2005

	Special Revenue
	Downtown Development Authority
REVENUES	
Taxes	\$ 52,288
Intergovernmental	334
Interest	<u>687</u>
TOTAL REVENUES	53,309
EXPENDITURES	
Current	
Community and economic development	<u>2,116</u>
EXCESS OF REVENUES OVER EXPENDITURES	51,193
Fund (deficit), beginning of year	(6,775)
Prior period adjustment	<u>22,395</u>
Fund balance, end of year	<u><u>\$ 66,813</u></u>

City of Montrose

Component Unit Fund

RECONCILIATION OF THE STATEMENT OF REVENUES,  
EXPENDITURES, AND CHANGES IN FUND BALANCE OF THE GOVERNMENTAL  
FUND TO THE STATEMENT OF ACTIVITIES - DOWNTOWN DEVELOPMENT AUTHORITY

Year Ended June 30, 2005

<b>Net change in fund balance - governmental fund</b>	<b>\$ 51,193</b>
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Amounts reported for governmental activities in the statement of activities are different because:

Capital outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts are:

Depreciation expense	<u>(4,911)</u>
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<b>Change in net assets of governmental activities</b>	<b><u>\$ 46,282</u></b>
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Principals

Dale J. Abraham, CPA  
Michael T. Gaffney, CPA  
Steven R. Kirinovic, CPA  
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**MANAGEMENT LETTER**

To the Honorable Mayor and  
Members of the City Council  
City of Montrose  
Montrose, Michigan

As you know, we have recently completed our audit of the records of the City of Montrose, Michigan as of and for the year ended June 30, 2005. In connection with the audit, we feel that certain changes in your accounting and administrative procedures would be helpful in improving management's control and the operational efficiency of the accounting and administrative functions. These suggestions are a result of our evaluation of the internal control and our discussions with management.

1. The City should escheat unclaimed property to the State of Michigan.

During our audit, it was noted that the City had outstanding checks listed on their General Fund bank reconciliation that were more than one (1) year old. The Michigan Public Act 29 of 1995 provides that the Department report and escheat unclaimed property to the State of Michigan. This issue had been noted and reported in our audit comments the last two years.

We suggest the City attempt to contact the payees in an effort to clear old outstanding checks. In the event that the rightful property owners cannot be located, we suggest the City review their unclaimed property and escheat funds to the State of Michigan as necessary.

2. The City should establish a capitalization threshold in order to track material assets purchased.

During the course of our audit, it was noted the City does not have a formal capitalization threshold policy in place. This policy would set forth a dollar threshold for items purchased by the City, which would be considered material, long-lived assets which should be capitalized and depreciated. To facilitate the implementation of GASB Statement No. 34, we discussed the dollar threshold with management, who determined that a "per unit" threshold of \$1,500 would be appropriate. This issue had been noted and reported in our audit comments last year.

We suggest the City Council adopt a capital asset policy through formal resolution and such approval be documented in the minutes to the Council meeting. We also suggest that the policy include a provision for the approval of capital asset disposals in order to strengthen the internal controls related to the sale or disposition of capital assets.

3. The City should monitor and amend budgets for applicable funds as necessary.

During the course of our audit, we noted one (1) instance where expenditures had been incurred in excess of amounts appropriated. This was noted in the General Fund. The budget variance noted was caused by an audit adjustment to appropriately reflect the financed purchase of a backhoe as an expenditure of the current fiscal year.

Michigan Public Act 621 of 1978, as amended, provides that the Council shall adopt formal budgets for the General and all Special Revenue funds and shall not incur expenditures in excess of the amounts appropriated. The budget must include all anticipated expenditures and the related revenue and fund equity to fund these expenditures.

We suggest that the City adopt and amend its budgets through Council resolution and monitor budgeted against actual expenditures.



4. The City should review the appropriateness of proprietary fund transfers.

During the course of our audit, it was noted that the Sewer Fund transferred \$430,000 to the Local Street Fund. This money was used in the local street fund to cover prior and current construction projects.

As noted in our audit comments last year, we consider the funding of local street construction projects with revenue generated by the sewer system to be an inappropriate and unallowable expenditure of the City's funds. Subsequent to our prior audit comment, the City obtained a legal opinion from Miller, Canfield, Paddock and Stone, P.L.C. who considered the transfer of surplus funds generated by the Sewer Fund to be a lawful expenditure of the City.

We suggest the City refrain from making any future transfers from utility funds for purposes other than operating and maintaining the utility systems. We also suggest that the City remain aware of the Bolt vs. City of Lansing case and the impact the creation of unreasonable surpluses have on the operation of utility funds.

5. The Council should amend the City's investment policy to address the disclosure requirements of GASB Statement No. 40.

During the course of our audit and through discussions with administration, it was noted that the City has not amended their investment policy to addresses the reporting requirements of GASB Statement No. 40.

Deposit and investment resources often represent significant assets of the City's funds. These resources are necessary for the delivery of the City's services and programs, or to carry out its fiduciary responsibilities. Effective for the year ended June 30, 2005, GASB Statement No. 40 is designed to inform financial statement users about deposit and investment risks that could affect the City's ability to provide services and meet its obligations as they become due.

We suggest the Council review their current investment policy and make the necessary amendments to address custodial credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. Such policies are required to be disclosed in the notes to the City's financial statements by GASB Statement No. 40.

These conditions were considered in determining the nature, timing, and extent of the audit tests to be applied in our audit of the financial statements. These conditions did not affect our report on the financial statements dated September 29, 2005.

This report is intended solely for the information of management and the Mayor and Members of the City Council of the City of Montrose and is not intended to be, and should not be, used by anyone other than these specified parties.

We wish to express our appreciation for the courtesy and cooperation extended to us during our audit. We are available to discuss any or all of these suggestions with you and to provide assistance in the implementation of improvements.

*Abraham & Gaffney, P.C.*

ABRAHAM & GAFFNEY, P.C.  
Certified Public Accountants

September 29, 2005